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SUBJECT: EGYPTIAN QIZ EXPORTS LEVEL OFF IN FIRST QUARTER
2008

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Sensitive but unclassified, not for Internet distribution.

¶1. (U) SUMMARY: Egyptian exports to the United States under the Qualified Industrial Zone (QIZ) agreement leveled off in the first quarter of 2008 to \$169 million USD. GOE and Government of Israel trade officials continued to push for QIZ expansion into Upper Egypt at the quarterly QIZ meeting in Cairo on May 19. Two non-textile companies were among those newly certified for QIZ export. Despite criticism of the program by opposition parliamentarians, the GOE continued to publicly seek foreign investment for QIZ factories. END SUMMARY.

¶2. (U) After QIZ exports dropped sharply in the last quarter of 2007 because of seasonal factors and sluggish US demand, QIZ exports rose in the first quarter of 2008 to a level 2-percent higher than the same period a year earlier, suggesting that exports under the three-year-old program are leveling off under current conditions. Israeli exports to Egypt under the agreement fell 8 percent to \$18 million, consistent with the GOE-GOI agreement in October 2007 to reduce the required level of Israeli content in Egyptian QIZ exports to 10.5 percent.

¶3. (U) At the quarterly meeting of the joint GOE-GOI QIZ committee May 19, GOE co-chair Sayed el-Bous and GOI co-chair Gabby Bar continued to argue in favor of QIZ expansion into Upper Egypt and asked about the status of the GOE-GOI request to USTR to approve expansion. We noted that USTR Susan Schwab and GOE Minister of Trade Rachid Rachid had discussed the issue in Sharm al-Sheikh on May 18 and that the request remained under active consideration.

¶4. (U) The GOE reported at the meeting that seven new companies had qualified for QIZ export: five textile producers, one food processor, and one tableware producer. The food company, Deyhydrofoods, told us after the meeting that they expect to begin exporting dried vegetables within several months and quadruple their current production by the end of 2009, thanks to the QIZ program. The company expects to purchase Israeli packaging material to meet the content requirement.

¶5. (U) El-Bous argued at the meeting that further reductions in the Israeli content requirement are necessary to encourage more non-textile companies to participate in the program because they cannot make economical use of the current required levels of Israeli inputs. Bar responded that the GOI will help any Egyptian industrialist having trouble finding enough Israeli content to locate appropriate Israeli suppliers.

¶6. (U) Regardless, the economics of the QIZ program continue to heavily favor textile producers, who account for more than 99 percent of QIZ exports. While more than 500 US companies have purchased QIZ products during the three years of the agreement, the top three companies -- Gap, Walmart, and Levi Strauss -- imported a third of all QIZ production, primarily jeans and other pants.

¶7. (U) The same day of the meeting, local press reported demands by 35 independent, Muslim Brotherhood, and opposition party parliamentarians for the GOE to freeze the QIZ agreement and other trade with Israel. Such demands have been routine throughout the life of the program, however. The next day, local press carried a statement by Ali Awni, head of the GOE QIZ unit, that the GOE is starting a campaign to encourage Eastern European investment in QIZ factories.

¶8. (SBU) Comment: The latest export results are consistent with our view that the QIZ agreement is maturing; the dramatic export growth rates of the first two years have come to an end (reftel). We believe that QIZ expansion into Upper Egypt is necessary to further expand the benefits of the agreement -- cooperation between Egypt and Israeli and creation of Egyptian jobs in a needy and restive region.
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